

INVESTMENT GUIDELINES FOR MISSOURI POLITICAL SUBDIVISIONS

*Recommendations for Implementing Recent
Missouri Statutory and Constitutional Changes*

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To all interested parties:

I am pleased to release the report *Investment Guidelines for Missouri Political Subdivisions: Recommendations for Implementing Recent Statutory and Constitutional Changes*. This report is intended to assist local agencies in implementing RSMo 30.950 including changes to the constitution through amendment 5. Additionally, this report includes a “model” investment policy which political subdivisions may find useful in writing a policy of their own.

As we experience changes at the federal and state level with regard to the investment of public funds, it is our obligation to stay abreast of these changes, take advantage of new techniques and opportunities, and maximize our earnings for the people we represent. As state treasurer, I have a responsibility to use my resources to aid local finance officers. I hope you will take advantage of this report to solidify your entity’s investment practices.

Sincerely,

Sarah Steelman
State Treasurer

**INVESTMENT GUIDELINES
FOR MISSOURI POLITICAL SUBDIVISIONS
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CHAPTER I. INVESTMENT POLICY

RSMo 30.950 (Appendix D) requires all political subdivisions to develop a written investment policy that must be adopted by the governing body of the political subdivision. A good investment policy drives the cash, treasury and investment management functions of an agency. It serves as a guide for setting and achieving program objectives, defines rules and establishes benchmarks, and reduces the exposure to liability of both the investment staff and governing board. Finally, it is also important to note that rating agencies pay attention to an agency's investment policy and portfolio in determining credit rating.

I. A. How should the investment policy be submitted to the governing body?

Recommendation: The investment policy should be an agenda item at a public meeting of the governing body of the political subdivision at some time prior to the year it covers. The policy should be thoroughly discussed by the governing body of the political subdivision and/or advisory body and approved by a vote of the governing body. The reason it is important to have a vote is to give "teeth" to the investment policy by increasing its authority and legitimacy.

I. B. Does a political subdivision have to adopt the “model” investment policy prepared by the state treasurer to be in compliance with RSMo 30.950?

No. The purpose of the model investment policy is to assist all Missouri political subdivisions in the preparation of an investment policy. The model investment policy is not intended to supplant an existing policy. Each entity should use the sample as a model to customize a policy to fit its needs, local laws, regulations, and other policies concerning the investment of public funds.

I. C. What must be included in the investment policy?

At a minimum, the investment policy must include the following components:

- (1) A commitment to the principles of safety, liquidity and yield, in that order, when managing public funds;
- (2) A prohibition on the purchase of derivative securities, either directly or through a repurchase agreement;
- (3) A prohibition on the use of leveraging whether through a reverse repurchase agreement or otherwise;
- (4) A prohibition on the use of public funds for speculation;
- (5) A requirement that on a regular basis the investments of the political subdivision shall be revalued to reflect prevailing market prices;
- (6) A requirement that investments which are downgraded below the minimum acceptable rating levels shall be reviewed for possible sale within a reasonable time period; and
- (7) A requirement that the current status and performance of the investments of the political subdivision be reported regularly to the governing body of the political subdivision.

I. D. Constitutional Amendment 5

Constitutional amendment 5 was approved by Missouri voters on November 3, 1998.

- 1) **How did amendment 5 change Article IV, section 15 (investment authority) of the Missouri constitution?**
The investment authority was expanded to include bankers' acceptances and commercial paper with maturities of not more than one hundred eighty days and possessing the highest rating issued by a nationally recognized rating agency. Additionally, the final maturity of treasury and agency security purchases was extended from three to five years.
- 2) **Is the investment authority of all political subdivision directly tied to Article IV, section 15 of the constitution?**
No, only the investment authority of school districts and counties.
- 3) **If a political subdivision currently has greater investment authority than the state treasurer, what course of action should be taken?**
The political subdivision should request a legal opinion from counsel regarding permitted investments. The auditor should sign off on the opinion and a written investment policy should then be developed based on those permitted investments. Finally, the governing body should adopt the policy.

CHAPTER II. FUNDS MANAGEMENT

Each person, treasurer, or governing body authorized to make investment decisions on behalf of political subdivisions is subject to the *prudent person standard*. These persons shall act with care, skill, prudence, and diligence under the circumstances then prevailing when investing and managing funds.

Risk is inherent throughout the investment process. There is risk assigned to any investment activity as well as opportunity risk related to inactivity. Market risk is derived from exposure to overall changes in the general level of interest rates while credit risk is the risk of loss due to the failure of the insurer of a security. The market value of a security varies inversely with the level of interest rates. If an investor is required to sell an investment with a 5 percent yield in a comparable 7 percent rate environment, that security will be sold at a loss. The magnitude of that loss will depend on the amount of time until maturity.

Another element of market risk is liquidity risk. Instruments with unique call features, special structures or those issued by little known companies are often thinly traded. Their uniqueness often makes finding prospective buyers in a secondary market more difficult and, consequently, the securities' marketability and price are discounted. However, under certain market conditions, gains are also possible with these types of securities.

Default risk occurs when the borrower is unable to repay the obligation. Generally, securities issued by the federal government and its agencies are considered the most secure, while securities issued by private corporations or negotiable certificates of deposit issued by commercial banks have a greater degree of risk. Securities with additional credit enhancements, such as bankers acceptances, collateralized repurchase agreements and collateralized bank deposits are somewhere between the two on the risk spectrum.

The vast majority of portfolios are managed within a buy and hold policy. Investments are purchased with the intent and capacity to hold that security until maturity. At times, market forces or operations may dictate swapping one security for another or selling a security before maturity. Continuous analysis and fine tuning of the investment portfolio are considered prudent investment management.

Recommendation: Include the list of permissible securities in the investment policy, and modify the list to meet the unique needs of each local agency. These modifications may include additional restrictions on the type and amount of specific authorized investments to reflect the risk tolerance of the agency.

II. A. Are all U.S. Agency bonds legal investments?

There has been a lot of discussion about the risky nature of certain products and derivatives issued by U.S. Agencies. These agencies offer both traditional fixed-income securities (bonds) as well as other more complex, often-customized products (including derivatives). Political subdivisions may invest in a range of securities issued by U.S. Agencies, such as the Federal National Mortgage Association (Fannie Mae), Government National Mortgage Association (Ginnie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), as well as obligations from the Student Loan Marketing Association (Sallie Mae), Tennessee Valley Authority (TVA), and other federal agencies or US government-sponsored enterprises (GSE). Obviously, it is the highly customized securities that present the greatest amount of risk.

Recommendation: Political subdivisions should institute restrictions that recognize the different characteristics of U.S. agency bonds. Generally, the higher rates of interest that some of the more customized offerings provide can be overshadowed by lower levels of liquidity and higher levels of risk. Investments in these types of products should only be entered into with a clear awareness, by both the legislative body and treasurer, of risks involved and only if the local agency's staff has sufficient expertise to manage such investments.

II. B. Do the new laws have an impact on the relationship between local agencies and outside investment management firms?

Recommendation: A finance officer or treasurer can delegate duties to an external money manager via a principal-agent relationship, but they cannot delegate authority or fiduciary responsibility. Contracts with external managers should allow managers to make specific decisions within an established framework. Treasurers should closely monitor the actions of these individuals to ensure they are consistent with the agency's investment policy and philosophy, and demand that external managers provide timely reports that comply with the requirements of the law (A good source for more information about using money managers is the Government Finance Officers Association (GFOA) publication, *An Introduction to External Money Management for Public Cash Management*).

CHAPTER III. REPORTING REQUIREMENTS

RSMo 30.950 requires all political subdivisions to file reports on the status of their investment portfolio with their respective governing body. The report may include the following information:

- 1) Investment type, issuer, maturity, par value, and dollar amount invested in all securities, investments, and monies held by the political subdivision;
- 2) The funds or investments managed by contracted parties;
- 3) A market value as of the date of the report and the source of the valuation;
- 4) A citation of compliance with the investment policy or an explanation for noncompliance; and
- 5) A statement of the ability or inability to meet expenditure requirements for six months, as well as an explanation of why money will not be available if that is the case.

III. A. Questions regarding market value.

1) **How to determine the market value of the portfolio.**

The legislation requires reporting the market value of the agency's portfolio. The National Association of State Treasurers (NAST) recommends that local entities obtain independent third party assessment of investments and risk. The most common, and often easiest, approach is to request pricing information from the agency's safekeeping service, custodial service, or trustee.

An alternative way to determine the value of securities in a portfolio is to perform an in-house analysis by collecting information from different sources such as dealer quotes, online computer information, and certain publications that provide price estimates. These sources may not be as up-to-date or accurate as a pricing service, but they offer a relatively inexpensive method to make price estimates.

Recommendation: The market valuation data in the report should represent the agency's best available information and fairly represent the value of the portfolio, in the judgment of the investment officer.

Obtain an independent valuation of the portfolio to provide the most unbiased method of reporting current market values. In situations where an agency's budget does not allow independent valuations, the agency should use the best available sources of market price information available. A system can be created to track prices from different sources over time to evaluate the sensitivity of price estimates, but there is no standard for accuracy.

Prices for securities are estimates that carry a certain degree of error regardless of the approach used and they will fluctuate due to market conditions over time.

2) Can cost or par values be used in-lieu of market values?

Recommendation: Utilize cost or par value only for narrowly-traded securities that are within six months of maturing and when reliable market value estimates are not readily available. Report the cost of the investment for certificates of deposit.

4) Should the report include market values for individual securities?

The market value of each security in a portfolio must be computed before determining the portfolio's overall market value. However, political subdivisions can either provide the market values of each holding or give one aggregate market value of the entire portfolio.

Recommendation: List the individual market value for each security in the report. This approach gives a more complete picture of the health of a portfolio and brings individual investment performance to the attention of those responsible for oversight. An agency concerned that listing detailed information about individual holdings may lead to second guessing and micro-management of the treasurer's decisions may choose to list an aggregate market value and append a footnote to the portfolio's overall market value stating that data on particular investments is available upon request.

CHAPTER IV. TREASURY OVERSIGHT COMMITTEES

It is not uncommon to find treasury oversight committees in counties, cities and other political subdivisions even though the law does not require them to have such a committee. An important issue in the decision to establish a committee is the level of discretion accorded the investment officer in making investment decisions. The more discretion, the greater the need for oversight procedures. However, even in situations where an agency has a great deal of discretion, some believe an oversight committee merely duplicates work that can be better performed by the governing board and/or auditors. Others support the view that an oversight committee provides valuable information to the investment staff and involves members of the community in an important government function. A treasury oversight committee typically consists of three to eleven-members appointed from the following categories:

1. Treasurer;
2. Auditor, controller, or finance director as the case may be; and
3. Up to five other members of the public.

Recommendation: Each political subdivision should consider for itself if an oversight committee is appropriate based on their current oversight procedures, complexity of their portfolio, frequency with which they purchase securities, and skill level of their staff.

MODEL INVESTMENT POLICY

FOR POLITICAL SUBDIVISIONS OF THE STATE OF MISSOURI

December 3, 1998

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MODEL INVESTMENT POLICY FOR POLITICAL SUBDIVISIONS OF THE STATE OF MISSOURI

Preparation

The state treasurer prepared the following model investment policy reflecting the principles set forth in RSMo 30.950. Any political subdivision, which formally adopts such a model investment policy, shall be deemed to be in compliance with RSMo 30.950.

Purpose

The purpose of this investment policy is to assist all Missouri political subdivisions in the preparation of an investment policy. This policy is not intended to supplant an existing policy. Each entity should use this sample as a model to customize a policy to fit its needs, local laws, regulations, and other policies concerning the investment of public funds.

Source

This policy was modeled in part after the model investment policies of the *Government Finance Officers Association of Missouri* and the *Municipal Treasurers' Association of the United States and Canada*.

Adoption Process

This "draft" policy was distributed to the *Missouri School Board Association*, the *Missouri Municipal League*, the *Government Finance Officers Association of Missouri* and the *Missouri County Treasurer's Association* on September 17, 1997. The state treasurer accepted comments on the draft policy through the summer of 1998. A final policy was released on August 10, 1998. The policy was revised upon the passage of constitutional amendment 5 on December 3, 1998.

This model policy should not be adopted without consultation with the [entity's] legal counsel. The policy was written as a general guideline by the State Treasurer's Office and specific sections of the policy must be tailored to the needs and objectives of the [entity].

MODEL INVESTMENT POLICY

I. Scope

This policy applies to the investment of all operating funds of the [entity]. Longer-term funds, including investments of employees' retirement funds and proceeds from certain bond issues, are covered by a separate policy.

1. Pooling of Funds

Except for cash in certain restricted and special funds, the [entity] will consolidate cash balances from all funds to maximize investment earnings. Investment income will be allocated to the various funds based on their respective participation and in accordance with generally accepted accounting principles.

2. External Management of Funds

Investment through external programs, facilities and professionals operating in a manner consistent with this policy will constitute compliance.

II. General Objectives

The primary objectives, in priority order, of investment activities shall be safety, liquidity, and yield:

1. Safety

Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.

a. Credit Risk

The [entity] will minimize credit risk, the risk of loss due to the failure of the security issuer or backer, by:

- ☞ Pre-qualifying the financial institutions, broker/dealers, intermediaries, and advisors with which the [entity] will do business.

- ☞ Diversifying the portfolio so that potential losses on individual securities will be minimized.

b. Interest Rate Risk

The [entity] will minimize the risk that the market value of securities in the portfolio will fall due to changes in general interest rates, by:

- ☞ Structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity.

- ☞ Investing operating funds primarily in short-term securities

2. Liquidity

The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by structuring the portfolio so that securities mature concurrent with cash needs to meet anticipated demands (static liquidity). Furthermore, since all possible cash demands cannot be anticipated, the portfolio should consist largely of securities with active secondary or resale markets (dynamic liquidity). A portion of the portfolio also may be placed in bank deposits or repurchase agreements that offer same-day liquidity for short-term funds.

3. Yield

The investment portfolio shall be designed with the objective of attaining a market rate of return throughout budgetary and economic cycles, taking into account the investment risk constraints and liquidity needs. Return on investment is of secondary importance compared to the safety and liquidity objectives described above. The core of investments are limited to relatively low risk securities in anticipation of earning a fair return relative to the risk being assumed. Securities shall not be sold prior to maturity with the following exceptions:

✍✍A security with declining credit may be sold early to minimize loss of principal.

✍✍A security swap would improve the quality, yield, or target duration in the portfolio.

✍✍Liquidity needs of the portfolio require that the security be sold.

III. Standards of Care

1. Prudence

The standard of care to be used by investment officials shall be the “prudent person” standard and shall be applied in the context of managing an overall portfolio. Investment officers acting in accordance with written procedures and this investment policy and exercising due diligence shall be relieved of personal liability for an individual security’s credit risk or market price changes, provided deviations from expectations are reported in a timely fashion to the governing body and the liquidity and the sale of securities are carried out in accordance with the terms of this policy.

Investments shall be made with judgement and care, under circumstances then prevailing, which persons of prudence, discretion and intelligence exercise in the management of their own affairs, not for speculation, but for investment, considering the probable safety of their capital as well as the probable income to be derived.

2. Ethics and Conflicts of Interest

Officers and employees involved in the investment process shall refrain from personal business activity that could conflict with the proper execution and management of the investment program, or that could impair their ability to make impartial decisions. Employees and investment officials shall disclose any material

interests in financial institutions with which they conduct business. They shall further disclose any personal financial/investment positions that could be related to the performance of the investment portfolio. Employees and officers shall refrain from undertaking personal investment transactions with the same individual with which business is conducted on behalf of the [entity].

3. Delegation of Authority

Authority to manage the investment program is granted to [designated official or external professional, hereinafter referred to as investment officer] and derived from the following [insert code citation, ordinances, charters, statutes or constitution]. Responsibility for the operation of the investment program is hereby delegated to the investment officer, who shall act in accordance with the established written procedures and internal controls for the operation of the investment program consistent with this investment policy. Procedures should include references to: safekeeping, delivery vs. payment, investment accounting, repurchase agreements, wire transfer agreements, and collateral/depository agreements. No person may engage in an investment transaction except as provided under the terms of this policy and the procedures established by the investment officer. The investment officer shall be responsible for all transactions undertaken and shall establish a system of controls to regulate the activities of subordinate officials.

IV. Investment Transactions

1. Authorized Financial Dealers and Institutions

A list will be maintained of financial institutions authorized to provide investment transactions. In addition, a list also will be maintained of approved security broker/dealers selected by creditworthiness as determined by the investment officer and approved by the governing body. These may include “primary” dealers or regional dealers that qualify under Securities and Exchange Commission (SEC) Rule 15C3-1 (uniform net capital rule).

All financial institutions and broker/dealers who desire to become qualified for investment transactions must supply the following as appropriate:

- ~~///~~ Audited financial statements.
- ~~///~~ Proof of National Association of Securities Dealers (NASD) certification.
- ~~///~~ Proof of state registration.
- ~~///~~ Completed broker/dealer questionnaire.
- ~~///~~ Certification of having read and understood and agreeing to comply with the [entity’s] investment policy.

An annual review of the financial condition and registration of qualified financial institutions and broker/dealers will be conducted by the investment officer.

From time to time, the investment officer may choose to invest in instruments offered by emerging or minority firms and community financial institutions. In such

situations, a waiver to the criteria under Paragraph 1 may be granted by the governing body. All terms and relationships will be fully disclosed prior to purchase and will be reported to the governing body of the [entity] on a consistent basis. The governing body of the [entity] should approve these types of investment purchases in advance.

2. Internal Controls

The investment officer is responsible for establishing and maintaining an internal control structure that will be reviewed annually with the [entity's] independent auditor. The internal control structure shall be designed to ensure that the assets of the [entity] are protected from loss, theft or misuse and to provide reasonable assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the cost of control should not exceed the benefits likely to be derived and (2) the valuation of costs and benefits require estimates and judgements by management.

The internal controls shall address the following points:

- ~~///~~Control of collusion.
- ~~///~~Separation of transaction authority from accounting and record keeping.
- ~~///~~Custodial safekeeping.
- ~~///~~Avoidance of physical delivery securities.
- ~~///~~Clear delegation of authority to subordinate staff members.
- ~~///~~Written confirmation of transactions for investments and wire transfers.
- ~~///~~Development of a wire transfer agreement with the lead bank and third party custodian.

3. Delivery vs. Payment

All trades where applicable will be executed by delivery vs. payment (DVP) to ensure that securities are deposited in eligible financial institutions prior to the release of funds. All securities shall be perfected in the name or for the account of the [entity] and shall be held by a third-party custodian as evidenced by safekeeping receipts.

V. Suitable and Authorized Investments

1. Investment Types

In accordance with and subject to restrictions imposed by current statutes, the following list represents the entire range of investments that [entity] will consider and which shall be authorized for the investments of funds by the [entity].

- a. United States Treasury Securities. The [entity] may invest in obligations of the United States government for which the full faith and credit of the United States are pledged for the payment of principal and interest.
- b. United States Agency Securities. The [entity] may invest in obligations issued or guaranteed by any agency of the United States Government as described in V. (2).

- c. Repurchase Agreements. The [entity] may invest in contractual agreements between the [entity] and commercial banks or primary government securities dealers. The purchaser in a repurchase agreement (repo) enters into a contractual agreement to purchase U.S. Treasury and government agency securities while simultaneously agreeing to resell the securities at predetermined dates and prices.
- d. Collateralized Public Deposits (Certificates of Deposit). Instruments issued by financial institutions which state that specified sums have been deposited for specified periods of time and at specified rates of interest. The certificates of deposit are required to be backed by acceptable collateral securities as dictated by State statute.
- e. Bankers' Acceptances. Time drafts drawn on and accepted by a commercial bank, otherwise known as bankers' acceptances. The [entity] may invest in bankers' acceptances issued by domestic commercial banks possessing the highest rating issued by Moody's Investor Services, Inc. or Standard and Poor's Corporation.
- f. Commercial Paper. The [entity] may invest in commercial paper issued by domestic corporations, which has received the highest rating issued by Moody's Investor Services, Inc. or Standard and Poor's Corporation. Eligible paper is further limited to issuing corporations that have total commercial paper program size in excess of five hundred million dollars (\$500,000,000).

2. Security Selection

The following list represents the entire range of United States Agency Securities that the [entity] will consider and which shall be authorized for the investment of funds by the [entity]. Additionally, the following definitions and guidelines should be used in purchasing the instruments:

- a. U.S. Govt. Agency Coupon and Zero Coupon Securities. Bullet coupon bonds with no embedded options.
- b. U.S. Govt. Agency Discount Notes. Purchased at a discount with maximum maturities of one (1) year.
- c. U.S. Govt. Agency Callable Securities. Restricted to securities callable at par only with final maturities of five (5) years.
- d. U.S. Govt. Agency Step-Up Securities. The coupon rate is fixed for an initial term. At coupon date, the coupon rate rises to a new, higher fixed term. Restricted to securities with final maturities of five (5) years.
- e. U.S. Govt. Agency Floating Rate Securities. The coupon rate floats off one index. Restricted to coupons with no interim caps that reset at least quarterly.

- f. U.S. Govt. Mortgage Backed Securities. Restricted to securities with final maturities of five (5) years.

3. **Investment Restrictions and Prohibited Transactions**

To provide for the safety and liquidity of the [entity's] funds, the investment portfolio will be subject to the following restrictions:

- a. Borrowing for investment purposes ("Leverage") is prohibited.
- b. Instruments known as Structured Notes (e.g. inverse floaters, leveraged floaters, and equity-linked securities) are not permitted. Investment in any instrument, which is commonly considered a "derivative" instrument (e.g. options, futures, swaps, caps, floors, and collars), is prohibited.
- c. Contracting to sell securities not yet acquired in order to purchase other securities for purposes of speculating on developments or trends in the market is prohibited.
- d. No more than 5% of the total market value of the portfolio may be invested in bankers' acceptances issued by any one commercial bank and no more than 5% of the total market value of the portfolio may be invested in commercial paper of any one issuer.

4. **Collateralization**

Collateralization will be required on two types of investments: certificates of deposit and repurchase agreements. The market value (including accrued interest) of the collateral should be at least 100%.

For certificates of deposit, the market value of collateral must be at least 100% or greater of the amount of certificates of deposits plus demand deposits with the depository, less the amount, if any, which is insured by the Federal Deposit Insurance Corporation, or the National Credit Unions Share Insurance Fund.

All securities, which serve as collateral against the deposits of a depository institution, must be safekept at a non-affiliated custodial facility. Depository institutions pledging collateral against deposits must, in conjunction with the custodial agent, furnish the necessary custodial receipts within five business days from the settlement date.

The [entity] shall have a *depository contract and pledge agreement* with each safekeeping bank that will comply with the Financial Institutions, Reform, Recovery, and Enforcement Act of 1989 (FIRREA). This will ensure that the [entity's] security interest in collateral pledged to secure deposits is enforceable against the receiver of a failed financial institution.

5. **Repurchase Agreements**

The securities for which repurchase agreements will be transacted will be limited to U.S. Treasury and government agency securities that are eligible to be delivered via the Federal Reserve's Fedwire book entry system. Securities will be delivered to the [entity's] designated Custodial Agent. Funds and securities will be transferred on a delivery vs. payment basis.

VI. Investment Parameters

1. Diversification

The investments shall be diversified to minimize the risk of loss resulting from over concentration of assets in specific maturity, specific issuer, or specific class of securities. Diversification strategies shall be established and periodically reviewed. At a minimum, diversification standards by security type and issuer shall be:

- a. U.S. treasuries and securities having principal
and/or interest guaranteed by the U.S. government..... 100%
- b. Collateralized time and demand deposits.....100%
- c. U.S. Government agencies, and government
sponsored enterprises.....no more than 60%
- d. Collateralized repurchase agreements.....50%
- e. U.S. Government agency callable securities.....no more than 30%
- f. Commercial Paper.....no more than 30%
- g. Bankers' Acceptances.....no more than 30%

2. Maximum Maturities

To the extent possible, the [entity] shall attempt to match its investments with anticipated cash flow requirements. Investments in bankers' acceptances and commercial paper shall mature and become payable not more than one hundred eighty days (180) from the date of purchase. All other investments shall mature and become payable not more than five (5) years from the date of purchase. The [entity] shall adopt weighted average maturity limitations that should not exceed three (3) years and is consistent with the investment objectives.

Because of inherent difficulties in accurately forecasting cash flow requirements, a portion of the portfolio should be continuously invested in readily available funds such as in bank deposits or overnight repurchase agreements to ensure that appropriate liquidity is maintained to meet ongoing obligations.

VII. Reporting

1. Methods

The investment officer shall prepare an investment report at least quarterly, including a management summary that provides an analysis of the status of the current investment portfolio and transactions made over the last quarter. This management summary will be prepared in a manner that will allow the [entity] to ascertain whether investment activities during the reporting period have conformed to the investment policy. The report should be provided to the governing body of the [entity]. The report will include the following:

- ~~1. Listing of individual securities held at the end of the reporting period.~~
- ~~2. Realized and unrealized gains or losses resulting from appreciation or depreciation by listing the cost and market value of securities over one-year duration (in accordance with Government Accounting Standards Board (GASB) 31 requirements). [Note, this is only required annually]~~
- ~~3. Average weighted yield to maturity of portfolio on investments as compared to applicable benchmarks.~~
- ~~4. Listing of investment by maturity date.~~
- ~~5. Percentage of the total portfolio which each type of investment represents.~~

2. Performance Standards

The investment portfolio will be managed in accordance with the parameters specified within this policy. The portfolio should obtain a market average rate of return during a market/economic environment of stable interest rates. A series of appropriate benchmarks may be established against which portfolio performance shall be compared on a regular basis.

Commercial paper and bankers' acceptances must be reviewed monthly to determine if the rating level has changed. The commercial paper and bankers' acceptances should be reviewed for possible sale if the securities are downgraded below the minimum acceptable rating levels.

3. Marking to Market

The market value of the portfolio shall be calculated at least quarterly and a statement of the market value of the portfolio shall be issued at least annually to the governing body of the [entity]. This will ensure that review of the investment portfolio, in terms of value and price volatility, has been performed.

VIII. Policy Considerations

1. Exemption

Any investment currently held that does not meet the guidelines of this policy shall be exempt from the requirements of this policy. At maturity or liquidation, such monies shall be reinvested only as provided by this policy.

2. Adoption

This policy shall be adopted by resolution of the [entity's] governing body. The policy shall be reviewed annually by the investment officer and recommended changes will be presented to the governing body for consideration.

IX. List of Attachments

The following documents, as applicable, are attached to this policy:

- ~~☐☐~~ Securities acceptable as collateral to secure deposits
- ~~☐☐~~ Listing of authorized personnel
- ~~☐☐~~ Relevant investment statutes and ordinances
- ~~☐☐~~ Repurchase agreements and tri-party agreements
- ~~☐☐~~ Listing of authorized broker/dealers and financial institutions
- ~~☐☐~~ Safekeeping agreements
- ~~☐☐~~ Wire transfer agreements
- ~~☐☐~~ Sample investment reports
- ~~☐☐~~ Glossary

Securities Acceptable as Collateral to Secure Deposits

STATE OF MISSOURI
OFFICE OF THE STATE TREASURER

**SECURITIES ACCEPTABLE AS COLLATERAL
TO SECURE STATE DEPOSITS**

The securities described below are hereby designated as acceptable collateral for state funds on deposit, as required by Section 30.270 RSMo (as amended). The State Treasurer reserves the right to refuse to accept as collateral any security or securities on this list, or to request the submission of an alternate acceptable security or securities, if, in the sole discretion of the State Treasurer, the State Treasurer determines that such action will provide greater security for the deposit of state funds.

The securities described below are designated as acceptablecollateral for the deposit of state funds. The listing isnot intended to serve as, and shouldnot be considered as a listing oflegally authorized investment instruments

1. Marketable Treasury securities of the United States.
2. The following debt securities of the State of Missouri and its state authorities:
 - a. General obligation debt securities issued by the State of Missouri.
 - b. Revenue bonds issued by the Missouri Board of Public Buildings or Department of Natural Resources.
 - c. Revenue bonds of the Missouri Housing Development Commission, Missouri Health and Education Facilities Authority, Missouri Higher Education Loan Authority, Missouri Environmental Improvement and Energy Resources Authority, Missouri Agricultural and Small Business Development Authority, Missouri Industrial Development Board, or state-owned educational institutions, so long as any of the above are rated "A" or better by Moody's or Standard & Poors (M1 on notes), or are secured by a federal agency guarantee (directly or through guaranteed loans).
3. General obligation bonds of any city in this state having a population of not less than two thousand.
4. General obligation bonds of any county of this state.
5. General obligation bonds, approved and registered, of any school district situated in this state.

6. General obligation bonds, approved and registered, of any special road district in this state.
7. General obligation state bonds of any of the 50 states.
8. Debt securities of the Federal Farm Credit System.
9. Debt securities of the Federal Home Loan Banks (FHLB) (excluding Zeros).
10. Other debt securities guaranteed by the United States or its agencies or instrumentalities, as follows:
 - a. Debt securities of the Federal National Mortgage Association (FNMA).
 - b. Debt securities of the Student Loan Marketing Association (SLMA).
 - c. Debt securities of the Government National Mortgage Association (GNMA).
 - d. Debt securities of the Federal Home Loan Mortgage Corporation (FHLMC) (excluding FHLMC Mortgage Cash Flow Obligations).
 - e. Guaranteed Loan Pool Certificates of the Small Business Administration (SBA).
 - f. Federal Home Administration insured notes (CBOs).
 - g. Public housing notes and bonds ("project notes and bonds") issued by public housing agencies, guaranteed as to the payment of principal and interest by the government of the United States or any agency or instrumentality thereof.
 - h. Debt securities of the Resolution Funding Corporation (REFCORP).

All pledges of pass-through mortgage-backed securities will be valued at 90% of market value. SBA pool certificates and collateralized mortgage obligations will be valued at 75% of market value. The only Collateralized Mortgage Obligations (CMO) the Treasurer's Office will accept are Planned Amortization Class (PAC) Collateralized Mortgage Obligations that have a weighted average life not to exceed three years and pass the FFIEC High Risk Stress Test. No Strips or Zeros are acceptable.

11. Bonds of any political subdivision established under the provisions of Section 30, Article VI, of the Constitution of Missouri.
12. Tax anticipation notes issued by any county of class one in Missouri.

13. Surety bonds issued by an insurance company licensed under the laws of the State of Missouri whose claims-paying ability is rated in the highest category by Duff & Phelps, A. M. Best, Standard & Poors, or Moody's. The face amount of such surety bond shall be at least equal to the portion of the deposit to be secured by the surety bond.
14. An irrevocable standby letter of credit issued by a Federal Home Loan Bank possessing the highest rating issued by at least one nationally recognized statistical rating agency.

Unless noted otherwise, the market value of collateral must be 100% or greater of the amount of state time deposits (including interest to maturity) plus demand deposits with the depository, less the amount, if any, which is insured by the Federal Deposit Insurance Corporation, or the National Credit Unions Share Insurance Fund. All securities pledged as collateral by the depository will be held by the Missouri State Treasurer, in a segregated account. All collateral pledged must be delivered in bearer form, book-entry form, or in the case of fully registered certificates, placed into the nominee name of the custodian.

Effective Date: August 28, 1998

GLOSSARY

GLOSSARY

As used in the attached model investment policy, the following terms shall mean:

Annual Review:

For the purpose of reviewing authorized financial dealers and institutions, annual review requires an investment officer to ensure that the financial dealer or institution is in compliance with the governing body's established procedures.

Banker's Acceptance (BA)

A short-term financial instrument that is the unconditional obligation of the accepting bank. Banker's acceptances, or Bas, arise from transactions involving the import, export, transit, or storage of goods – domestic as well as international transit. For investors, it is important to realize that the underlying transaction that gives rise to a BA is almost completely irrelevant to the credit quality or the liquidity of the instrument. The actual BA is created at a late stage in the underlying transaction when a bank accepts its obligation to pay the holder of the accepted draft. In other words, when the transaction becomes a BA it becomes an unconditional obligation of the accepting bank. From an investor's point of view, a BA is a bank obligation that has at least the same credit strength as any CD issued by the same bank. In fact, BAs are typically stronger than CDs because in addition to the credit strength of the accepting bank they are backed by the credit strength of a drawer; an endorsing bank, if one is involved in the transaction; and usually by the pledge of documents representing ownership of the trade goods and insurance on the goods. BAs do not, however, carry federal deposit insurance. BAs are considered safe, liquid, short-term money market investments.

Bond Proceeds

The money paid to the issuer by the purchaser or underwriter of a new issue of municipal securities. These moneys are used to finance the project or purpose for which the securities were issued and to pay certain costs of issuance as may be provided in the bond contract.

Broker

A party who brings buyers and sellers together. Brokers do not take ownership of the property being traded. They are compensated by commissions. They are not the same as dealers; however, the same individuals and firms that act as brokers in some transactions may act as dealers in other transactions.

Callable Bond

A bond that the issuer has the right to redeem prior to maturity. Some callable bonds may be redeemed on one call date while others have multiple call dates. Some callable bonds may be redeemed at par while others can only be redeemed at a premium.

Certificate of Deposit (CD)

A deposit of funds, in a bank or savings and loan association, for a specified term that earns interest at a specified rate or rate formula. They may be for terms as short as 1 week or as long or longer than 10 years.

Commercial Paper

Unsecured, short-term promissory notes issued by corporations for specific amounts and with specific maturity dates. Firms with lower ratings or firms without well-known names usually back their commercial paper with guarantees or bank letters of credit. Commercial paper may be sold on a discount basis or may bear interest. Terms can be as short as 1 day and usually do not exceed 270 days.

Custodial Agent:

An entity that holds collateral for deposits with financial institutions, investment securities, or securities underlying repurchase agreements.

Delivery vs. Payment (DVP)

The simultaneous exchange of securities and cash. The safest method of settling either the purchase or sale of a security. In a DVP settlement, the funds are wired from the buyer's account and the security is delivered from the seller's account in simultaneous, interdependent wires.

GASB 31

Statement No. 31 of the Governmental Accounting Standards Board: Accounting and Financial Reporting for Certain Investments and for External Investment Pools, establishes accounting standards for securities owned by governmental entities.

Government Accounting Standards Board (GASB)

An accounting industry organization; part of the Financial Accounting Foundation. GASB issues statements of accounting standards that define and govern GAAP for state and local government entities in the United States.

Mark to Market

The process of restating the carrying value of an asset or liability to equal its current market value.

Market Value

The price at which a security is trading and presumably could be purchased or sold at a particular point in time.

Maturity

The date on which the principal or stated value of an investment becomes due and payable.

Operating funds

Includes all investable funds of the political entity with the exception of bond proceeds, retirement funds and self-insurance funds. Investable funds shall include all fund balances and surplus funds.

Par Value

The amount of principal which must be paid at maturity. Also referred to as the face amount of a bond, normally quoted in \$1,000 increments per bond.

Repurchase Agreement (RP)

A form of secured, short-term borrowing in which a security is sold with a simultaneous agreement to buy it back from the purchaser at a future date. The purchase and sales agreements are simultaneous, but the transactions are not. The sale is a cash transaction while the return purchase is a forward transaction since it occurs at a future date. The seller/borrower pays interest to the buyer at rate negotiated between the parties. Rates paid on repos are short-term money market interest rates and are completely unrelated to the coupon rate paid on the instrument being purchased. Informally known as repos.

Safekeeping

An arrangement under which a third party holds securities or other valuables under safe, controlled conditions. A safekeeping arrangement is evidenced by a safekeeping receipt.

Swap

The sale of one or more securities in order to purchase one or more different securities with the proceeds from the sale. Bond swaps usually take advantage of changes in market conditions or more favorable investment characteristics. For example, swaps are often done to lengthen or shorten maturities when investors change their outlook for future rates.

US Treasury Obligations

Debt obligations of the United States Government sold by the Treasury Department in the forms of Bills, Notes, and Bonds. Bills are short-term

obligations that mature in 1 year or less and are sold on the basis of a rate of discount. Notes are obligations that mature between 1 year and 10 years. Bonds are long-term obligations that generally mature in 10 years or more.

Weighted Average Maturity (WAM)

The average maturity of all the securities that comprise a portfolio that is typically expressed in days or years.

RSMo 30.950

MISSOURI STATUTES

Missouri Revised Statutes

Chapter 30 **State Treasurer** **Section 30.950**

August 28, 1999

Definitions--written investment policy required--state treasurer's duty.

30.950. 1. As used in this section, the following terms shall mean:

- (1) "Derivative securities", a financial instrument, contract or obligation which has a value or return based upon or linked to another asset or index, or both, separate from the financial instrument, contract or obligation itself;
- (2) "Governing body", the board, body or persons in which the powers of a political subdivision as a body corporate, or otherwise, are vested;
- (3) "Leveraging", using current assets as collateral to purchase other assets;
- (4) "Political subdivision", any agency or unit of this state;
- (5) "Speculation", contracting to sell securities not yet acquired in order to purchase other securities for purposes of speculating on developments or trends in the market.

2. Every political subdivision of this state which is responsible for the management and investment of public funds and which has existing authority to invest such funds in a manner other than in depositary accounts at financial institutions in this state shall promulgate, formally adopt and comply with a written investment policy containing, but not be limited to, the following components:

- (1) A commitment to the principles of safety, liquidity and yield, in that order, when managing public funds;
- (2) A prohibition on the purchase of derivative securities, either directly or through a repurchase agreement;
- (3) A prohibition on the use of leveraging whether through a reverse repurchase agreement or otherwise;
- (4) A prohibition on the use of public funds for speculation;

- (5) A requirement that on a regular basis the investments of the political subdivision shall be revalued to reflect prevailing market prices;
 - (6) A requirement that investments which are downgraded below the minimum acceptable rating levels shall be reviewed for possible sale within a reasonable time period; and
 - (7) A requirement that the current status and performance of the investments of the political subdivision be reported regularly to the governing body of the political subdivision.
- 3. The state treasurer shall prepare a model form of an investment policy reflecting the principles set forth herein which shall be made available to political subdivisions in the state. Any political subdivision which formally adopts such a model investment policy shall be deemed to be in compliance with the requirements of this section.
 - 4. Notwithstanding any other law to the contrary, any political subdivision of the state which manages and invests public funds, but does not promulgate, formally adopt and comply with a written investment policy as described herein shall have its investment authority limited to those investments authorized by law as of January 1, 1997. Except for those political subdivisions authorized by law to place public funds in the investments authorized by section 15, article IV of the Constitution of Missouri, and only then if the political subdivision complies with the requirements of this section, nothing in this section shall be deemed to expand the investment authority of a political subdivision beyond that currently permitted by law.
 - 5. Any written investment policy promulgated and adopted in accordance with this section shall be deemed a public record.